

# **Drop the debt - go back to first principles: A challenge to the G7**

The G7's grand promise at Cologne – an enhanced HIPC that would deliver debt relief to 25 countries this year – has been left hanging. Only eight countries have begun to receive debt relief. IMF conditionality and an unnecessarily bureaucratic process has slowed debt relief to a trickle. Oxfam proposes a quicker, simpler way forward.

21 July 2000



Last year when G7 leaders met in Cologne, they promised that 25 countries would enter the reformed Highly Indebted Poor Country Initiative (HIPC) by the end of 2000. However, only eight countries have started to receive finance under the initiative. At their meeting in Okinawa 21-23<sup>rd</sup> July, the G7 will have to face up to the challenge of speeding up the implementation of HIPC. Without progress, the human development needs of some of the world's poorest countries will be denied.

Oxfam believes that the G7 leaders should go back to first principles. In Cologne they agreed to provide increased debt relief, more quickly, and to link it to poverty reduction. Unfortunately the IMF and World Bank have created a bureaucratic process that is delaying progress in the name of poverty reduction. The human costs of such delays are immense. HIPC countries have some of the lowest human development indicators in the world, coupled with serious resource constraints. UNICEF estimates that HIPC countries are so far off-track on meeting targeted reductions in child mortality, that the gap between projected child mortality and current trends represents around 2 million additional child deaths in 2015.

The potential short-term benefits from debt relief are being lost. Countries are being locked into a broader macroeconomic reform agenda, including privatisation and trade liberalisation. No one would deny the need for reform, but a way must be found to provide the immediate benefits of debt relief. Lessons can be learnt from Uganda's experience. Early in the HIPC process the government established a Poverty Action Fund (PAF), transparently managed and audited, through which it channelled debt relief resources to finance human development goals. This has allowed for increased expenditures in school construction, as part of efforts to achieve universal primary education, or to increased expenditures in water supply, an area raised as a priority concern during nation-wide consultations with the poor. More recently Honduras proposed this approach, creating a Poverty Reduction Support Fund to utilise HIPC finance. The advantages of these approaches are threefold:

- They provide a direct budget facility to support clearly defined and monitorable poverty reduction goals.
- They provide a point of contact between government and civil society, and also donors.
- Application of auditing and other transparency measures promote wider budget management goals.

Of course such an approach is not without its problems, including that of fungibility. It also goes without saying that a Poverty Action Fund is no substitute for a broader poverty reduction strategy, including a poverty focused macroeconomic framework. But it does offer a credible alternative to the current framework, and could provide the opportunity to speed the process of delivering debt relief resources for poverty reduction efforts.

**We propose that all countries enter HIPC2 immediately, if they meet one condition:**

- **Commitment to placing debt relief finance into a transparently managed Poverty Fund, as part of the Interim Poverty Reduction Strategy Paper (PRSP), which directs expenditure towards poverty reducing areas such as education, health, rural roads, employment generation programmes etc.**

The G7 Finance Ministers have already met, and have come up with very little. A proposal from the UK Chancellor to reward those countries at war, or in conflict, with speedier debt relief if they halt such conflicts, received support from other Finance Ministers. This is positive, but it is aimed at countries such as Burundi, the Democratic Republic of the Congo, Ethiopia, Sierra Leone, Liberia, Somalia, and Sudan - countries with serious and long-term conflict, where peace could take a very long time. Unfortunately the G7 have not addressed the key problem of why HIPC is going so slowly. Instead they need to look hard at the IMF and the World Bank; institutions they dominate as the largest shareholders. The majority of countries are being delayed for two key reasons:

### **1. IMF reforms delay debt relief:**

The IMF is tying progress on HIPC to the introduction of wide ranging economic reforms, thus delaying debt relief, rather than linking it to a direct poverty reduction agenda.

Several countries have suffered as a consequence of this approach. For instance, debt relief in Honduras was delayed while agreements were reached on the speed of privatisation of the electricity sector. Such issues are clearly important; subsidies to state owned enterprises are frequently not pro-poor, and many countries are challenged by such reforms. However, should problems around agreement on these issues stop progress on debt relief? The answer is no. Not if the intention is to achieve immediately tangible benefits to the poor.

While debt relief is delayed until agreement is reached on the reform programme, many of the reforms themselves are not reviewed for their impact on the poor. Currently there is no debate around pro-poor design of reforms, or the trade-offs between one reform or another with respect to their impact on poverty reduction efforts. There is also no serious effort to re-design, or adjust the sequence of reforms, if the poor are adversely affected.

### **2. Interim PRSPs are unnecessarily excessive:**

While progress in HIPC relies on IMF approval of the reform programme, it also relies on IMF and World Bank approval of an Interim PRSP. This is part of the process of linking debt relief to poverty reduction, but unfortunately it is being implemented in a way which is preventing debt relief from contributing to poverty reduction. The Interim

PRSP is supposed to be a 'light' document, providing a road map for how countries would reach a full PRSP, demonstrating a government's commitment to poverty reduction. Unfortunately Interim PRSPs are being developed in a slow and bureaucratic process, with confused direction from the IMF and World Bank, resulting in unnecessarily large and complex documents, further delaying progress and debt relief.

## How to speed up the HIPC process?

- **Immediate debt relief to countries which commit to a 'Poverty Fund' in the Interim PRSP:** Governments which produce an Interim Poverty Reduction Strategy paper providing details of the workings of a Poverty Fund, and which are committed to progressing towards broad macroeconomic stability, should be provided with immediate interim debt relief. This should become the Decision Point in HIPC2.

The Poverty Fund would detail how debt relief finance would be allocated to priority areas in the budget for poverty reduction. It would be monitored by civil society and by donors. Obvious priority areas would include health, education, rural roads, water supply, employment generation programmes and so on. The Interim PRSP should be a brief document, summarising how the government intends to develop a full PRSP, and how it intends to use debt relief resources in the interim period. Such a document could be prepared quickly, and should become the key document for judging progress in HIPC. This could mean that countries further behind in HIPC, such as Zambia or Nicaragua, could enter the framework within the next few months.

- **IMF policy recommendations to become part of a larger process focussed on growth, equity and poverty reduction:** While macroeconomic stability is important for poverty reduction, the IMF should take into account longer-term poverty challenges when agreeing Poverty Reduction and Growth Facilities (PRGF) with HIPC countries, and in reviewing progress under a PRGF. The World Bank should help more with this process. **If the country is broadly on track, the onus should be on the IMF to demonstrate clearly, and publicly, why debt relief, provided into a 'Poverty Fund' would not contribute to poverty reduction. If this cannot be done, then interim debt relief should be provided.**
- **Urgently review all countries:** We propose that all HIPC countries, including non-HIPC countries that have serious debt problems and poverty reduction challenges, such as Nigeria or Haiti, should be reviewed by the IMF and the World Bank by the time of their Prague Annual Meetings in September 2000. This process should be transparent, with explanations given as to why countries are denied debt relief. The IMF and World Bank HIPC teams will need additional staffing to urgently to accelerate this process. G7 countries could second staff to reinforce these teams.
- **War-affected countries:** Countries affected by war should not be able to divert the benefits of debt relief away from poverty reduction. However, country cases are rarely black or white. They all require careful judgement. Creditors would need to determine whether military spending is reasonable defence expenditure, or being

used for aggression - internationally, or internally. The extent of military expenditure would need to be addressed, and whether conflict is undermining planned public expenditure, particularly expenditure directed at poverty reduction. Overall, budgets would have to be transparent. If this assessment is positive and if the structure of the Poverty Fund is robust, and prioritised in poverty reducing areas, then debt relief should go ahead.

- **Governance:** It is not only war affected countries that raise issues for HIPC implementation. Countries which are not committed to poverty reduction, or where there are serious governance problems, would find it difficult to prioritise debt relief spending to commitments defined within a Poverty Fund, or to manage the fund in a transparent way. Without being able to demonstrate such commitments, debt relief should not be provided, since finance would be diverted and misused.

Oxfam International is a network of eleven aid agencies working in 120 countries throughout the developing world: Oxfam America, Oxfam in Belgium, Oxfam Canada, Community Aid Abroad (Australia), Oxfam Great Britain, Oxfam Hong Kong, Intermon (Spain), Oxfam Ireland, Netherlands Organization for International Development Cooperation (NOVIB), Oxfam New Zealand, and Oxfam Quebec. Please contact any of the agencies for further information.

<p><b>Oxfam International Advocacy Office</b> 733 15<sup>th</sup> Street NW, Suite #340 Washington, DC 20005, USA 1.202.783.3331 (ph) 1.202.783.5547 (fax) advocacy@oxfaminternational.org</p>	<p><b>Oxfam America</b> 26 West St. Boston, MA 0211-1206 1.617.482.1211 (ph) 1.617.728.2595 (fax) info@oxfamamerica.org</p>	<p><b>Oxfam Canada</b> Suite 300-294 Albert St. Ottawa, Ontario Canada K1P 6E6 1.613.237.5236 (ph) 1.613.237.0524 (fax) enquire@oxfam.ca</p>
<p><b>Oxfam-in-Belgium</b> Raadstraat 39 39 Rue du Conseil 1050 Brussels Belgium  32.2.512.9990 (ph) 32.2.514.2813 (fax) oxfamsol@oxfamsol.be</p>	<p><b>Oxfam Hong Kong</b> 9/F, Breakthrough Centre 191 Woosung Street Jordan, Kowloon Hong Kong 852.2520.2525 (ph) 852.2789.9545 (fax) info@oxfam.org.hk</p>	<p><b>Community Aid Abroad</b>  National &amp; Victorian Offices 156 George St. (Corner of Webb Street)  Fitzroy, Victoria Australia 3065 61.3.9289.9444 (ph) 61.3.9419.5318 (fax) enquire@caa.org.au</p>
<p><b>Oxfam Great Britain</b> 274 Banbury Road Oxford England OX2 7DZ 44.1865.311.311 (ph) 44.1865.312.600 (fax) oxfam@oxfam.org.uk</p>	<p><b>Oxfam New Zealand</b> P.O. Box 68-357 Newton Auckland 1032, New Zealand 64.9.355 6500 (ph) 64.9.355 6505 (fax) oxfam@oxfam.org.nz</p>	<p><b>Intermon</b> Roger de Lluria, 15 08010 Barcelona, Spain 34.3.482.0700 (ph) 34.3.482.0707 (fax) intermon@intermon.org</p>
<p><b>Oxfam Ireland Northern Ireland</b> 52-54 Dublin Road Belfast BT2 7HN  44.1232.230220 (ph) 44.1232.237771 (fax) <b>Republic of Ireland</b> 9 Burgh Quay Dublin 2, Ireland 35.31.672.7662 (ph) 35.31.672.7680 (fax)</p>	<p><b>Netherlands Organization for International Development Cooperation (NOVIB)</b> PO Box 30919 2500 GX The Hague, The Netherlands 31.70.342.1621 (ph) 31.70.361.4461 (fax)] info@novib.nl</p>	<p><b>Oxfam Quebec</b> 2330 rue Notre-Dame Ouest Bureau 200 Montreal, Quebec, Canada H3J 2Y2 1.514.937.1614 (ph) 1.514.937.9452 (fax) info@oxfam.qc.ca</p>

Published by Oxfam International July 2000

Published by Oxfam GB for Oxfam International under ISBN 978-1-84814-322-7